UNITED NATIONS

TD

United Nations Conference on Trade and Development

Distr.
GENERAL

TD/B/SCP/14
TD/B/SCP/AC.1/3
24 August 1995

Original: ENGLISH

TRADE AND DEVELOPMENT BOARD
Special Committee on Preferences
Twenty-second session
Geneva, 23 October 1995
Item 3 of the provisional agenda

# REPORT OF THE INTERGOVERNMENTAL GROUP OF EXPERTS ON RULES OF ORIGIN

Held at the Palais des Nations, Geneva
from 19 to 21 July 1995

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GE.95-52905 (E)

## INTRODUCTION

1. The Intergovernmental Group of Experts on Rules of Origin held its session from 19 to 21 July 1995 at the Palais des Nations, Geneva. In the course of the session, the Group of Experts held four plenary meetings and a number of informal meetings.

A. Opening statement

2. The **Officer-in-charge of the International Trade Division** stated that the Intergovernmental Group of Experts had an important task before it, having been convened by the Trade and Development Board at the request of the Special Committee on Preferences to make proposals on the harmonization, simplification and improvement of the GSP rules of origin in view of the policy review on the GSP to be conducted by the Special Committee at its twenty-second session (23 to 27 October 1995). The issue before the Group had been discussed at length in the sessional committee on rules of origin, but progress had been modest, especially on harmonization.

3. Since the introduction of the rules of origin, two major rounds of multilateral trade negotiations had taken place during which MFN rates of duty had been drastically reduced, thereby eroding preferential margins provided by GSP schemes. In the post-Uruguay Round era, GSP rules of origin might become a major obstacle to the full utilization of the GSP system because, with GSP preferential margins in some sectors being considerably reduced, the economic value of this margin might well be offset by the cost of complying with unnecessarily strict rules of origin. In fact, the existing rules of origin had been conceived against a background of industrial development and trade flows which no longer existed. In some cases, specific origin requirements for certain categories of product might not even be met by the same industries in preference-giving countries. Even trade preferences that provided for completely free-market access were not sufficient to stimulate the expected trade effects and economies of scale unless accompanied by liberal rules of origin which would allow for the exploitation of the trading opportunities created by those preferences.

4. He further observed that even in the GATT context, there had been a lack of multilaterally agreed rules and therefore different origin criteria were being applied by major trading nations. The recognition by these nations during the Uruguay Round that clear and predictable rules of origin would facilitate the flow of international trade, and that uniform criteria for rules of origin were needed to avoid unnecessary obstacles to trade, had led to the conclusion of the Agreement on Rules of Origin. This Agreement provided for the harmonization of non-preferential rules of origin according to a work programme to be carried out by a Technical Committee set up under the World Customs Organization. The content of the Agreement concerned only non-preferential rules of origin. Preferential rules of origin were dealt with by a Common Declaration that aimed at imparting transparency and predictability to preferential origin determination. Nevertheless, the work conducted by the Technical Committee on the concept of substantial transformation might produce results relevant for progress towards harmonization and simplification of the GSP rules of origin.

5. He stressed that, at this time, when proposals were being made to revitalize the GSP in the context of the 1995 policy review, GSP rules of origin should be the object of decisive improvements in line with the results obtained in the non-preferential area. Thus, the secretariat report on rules of origin (TD/B/SCP/AC.1/2) examined the World Trade Organization's (WTO) Agreement on Rules of Origin and made specific proposals for progress aimed at the harmonization, simplification and improvement of the GSP rules of origin in the light of the provisions contained in that Agreement and in the Common Declaration concerning preferential rules of origin.

## Chapter I

### CONSULTATIONS ON HARMONIZATION OF THE RULES OF ORIGIN

(Agenda item 3)

**and**

### CONSULTATIONS ON SIMPLIFICATION AND IMPROVEMENT OF THE RULES OF ORIGIN

(Agenda item 4)

6. For its consideration of these two items, the Group of Experts had before it the following documentation:

"Harmonization, simplification and improvement of the rules of origin: options and proposals for harmonization, simplification and improvement of the rules of origin" - study by the UNCTAD secretariat (TD/B/SCP/AC.1/2);

"Harmonization, simplification and improvement of the rules of origin: summary of replies received from preference-giving and preference-receiving countries to the questionnaire prepared by the UNCTAD secretariat" (TD/B/SCP/AC.1/2/Add.1).

7. The **representative of the UNCTAD secretariat** said that the Uruguay Round Agreement on Rules of Origin had for the first time brought non-preferential rules of origin within the scope of multilateral discipline. The Agreement aimed at harmonizing these rules through a detailed procedure involving the World Customs Organization (WCO). It also specified that the harmonized set of rules should be used to determine origin for all purposes related to the multilateral agreements on trade in goods. However, preferential rules of origin, of which the GSP was a part, had not been made part of the Agreement nor of the harmonization programme it contained. Instead, they were referred to in a Common Declaration. The study prepared by the secretariat examined the content of the Common Declaration within the GSP perspective and concluded that, as far as rules of origin in the GSP context were concerned, the Declaration represented a kind of standstill obligation, with two notable exceptions. The first concerned a procedure through which individuals might obtain from preference-giving countries prior binding origin information related to specific products that they might wish to export in order to determine whether or not these products were eligible for GSP treatment. The second exception concerned the judiciary review, i.e. the possibility to challenge in court the origin determination made by preference-giving authorities. In progressing towards improvements aimed at imparting stability and predictability to origin determination, the study recommended the swift implementation, in a consistent manner, of these two mechanisms.

8. As far as direct consignment and documentary evidence were concerned, the quest for simplification of these requirements had been considered to be the most suitable approach. It was felt that improvement of the rules of origin could be best achieved by increasing the scope for cumulation and donor-country content. However, the key area for discussions during the 1995 policy review was the complete harmonization of origin criteria under the GSP. The forthcoming harmonization of non-preferential rules of origin had a bearing on the crucial debate on whether possible harmonization of GSP rules should be based on the percentage criterion or the process criterion. The clear adoption of the process criterion in the context of the non-preferential rules of origin would undoubtedly contribute to resolving the dispute and provide scope for harmonization.

9. Under the World Trade Organization (WTO) Agreement on Rules of Origin, the work of the Technical Committee consisted in elaborating a harmonized set of non-preferential rules of origin. The purpose of, and one of the major difficulties in, developing such a harmonized set of rules of origin was to define the amount of working or processing which could be regarded as "substantial transformation". This finding applied irrespective of the non-preferential or preferential character of the harmonized set of rules to be elaborated. Thus, the work to be undertaken by the Technical Committee would be analogous to that which should be carried out for GSP rules of origin. The secretariat study suggested that the value and the technical nature of this exercise should be exploited and, where possible, translated into the GSP context. The UNCTAD secretariat would, therefore, follow the work of the Technical Committee as an observer and report on the results. On the basis of the outcome of the work done by the Technical Committee, preference-giving and preference-receiving countries might wish to pursue further the quest and prospects for harmonizing GSP rules of origin, against this solid and practical background. Once the harmonized set of rules of origin had been elaborated by the Technical Committee, such work would be presented to the Special Committee on Preferences for its consideration, with a view to progressing towards harmonization of GSP rules of origin.

10. In conclusion, he pointed to a number of other proposals concerning simplification and improvement of the rules of origin, namely, relaxation of transshipment rules, abolition of the requirements concerning the quality of paper of GSP Form A, updating of the notes on the back of GSP Form A, enlargement of origin cumulation rules to other forms of cumulation, and strengthening of administrative cooperation.

11. The representative of **China** said that the secretariat had made timely proposals for harmonizing, simplifying and improving the rules of origin. He noted that the reduction of duties agreed on by the preference-giving countries during the Uruguay Round negotiations would further narrow the preferential scope of the GSP. Different sets of rules of origin with low preferential duties would have a negative impact on the application and significance of the GSP in promoting the economic development of developing countries. He agreed that the adoption of the process criterion in non-preferential rules of origin would help to settle disputes as to whether the process criterion or the percentage criterion should be adopted in the GSP rules of origin.

12. There were now 13 sets of rules of origin. Although they could be included in two categories, i.e. the percentage criterion and the process criterion, the same product might have to apply to both criteria. The only way to solve this problem would be to adopt an integrated set of rules of origin - i.e. the process criterion - because it would be much easier to utilize the process criterion to ascertain substantial transformation since materials from outside the country of origin could be dealt with easily. The percentage criterion determined substantial transformation according to the ratio of the price of materials to the price of products, but both were affected by market fluctuations. The price was adjustable and could be concealed by artificially imposed factors. However, the process criterion needed to be improved. The European Union, Japan, Norway and Switzerland had all adopted the process criterion, but their process lists were different, and the same product was subject to different conditions specified in the various lists. An integrated process list should therefore be developed. If an integrated origin criterion, namely, the process criterion, could not be adopted, he suggested that the process criterion and the percentage criterion be unified. This unified process criterion would use the same process list that had been greatly simplified. The unified percentage criterion would stipulate that the price of contents from outside the country of origin should not exceed 50 per cent of the f.o.b. price of the end product, as the f.o.b. price could be accurately determined.

13. He considered that, with a view to encouraging more extensive economic and trade cooperation between preference-receiving countries and between preference-receiving and preference-giving countries, both "donor country content" and "global cumulation" should be accepted by all preference-giving countries concerned. Noting that, in general, products exported under the GSP were transhipped through a third party as most of the preference-receiving countries were not able to ship the products directly, he suggested that preference-giving countries abolish direct consignment and stipulate that, if exporters from preference-receiving countries filled in the third column of Form A designating the port of preference-giving countries as the destination port, the exports would be granted GSP treatment.

14. With regard to documentary evidence, he stated that Form A was necessary to obtain GSP treatment, but that the requirements for filling in Form A should be simplified and unified: i.e. they should stipulate the period of validity, verify whether the re-issued or the post-issued certificates were valid, and note that the second column of Form A may or may not be filled in depending on the needs of international trade.

15. In conclusion, he hoped that the consensus on harmonization, simplification and improvement would be reached during this meeting and that a new and acceptable set of rules of origin would be adopted.

16. The representative of the **European Community** stated that he approved the effort undertaken by UNCTAD to harmonize and simplify the GSP rules of origin, and that he was ready to discuss the points raised in the secretariat documentation. He was particularly pleased to see that such a large number of

representatives from both preference-giving and preference-receiving countries were attending the meeting of the Group of Experts. This would facilitate a better understanding of the difficulties faced by both groups of countries with a view to arriving at favourable conclusions.

17. The representative of **Switzerland** recalled that the purpose of the rules of origin was to ensure that the benefits of the GSP went to the rightful beneficiaries of the system, to the exclusion of others. Two factors were necessary to achieve this: (i) that certain production should take place in the beneficiary country under particular, well-defined circumstances; (ii) that trade deflection, whereby goods transiting through non-beneficiary countries could lay claim to preferences, should be avoided. In this connection, four fundamental questions could be raised:

(1) To what extent was it rational to maintain two major origin systems, one based on minimum local content (as in the United States, Australia, New Zealand), the other on the change of tariff heading and/or maximum imported materials (as in Canada, the European Union, EFTA, Japan)?

(2) To what extent were the rules applied to specific products and contained in the lists adapted to the industrial base in developing countries, and to what extent could such rules lead to trade distortion in trade flows?

(3) What effect did the different cumulation rules have on the aptitude of developing countries to comply with the origin requirements?

(4) To what extent were the rules of origin adapted to the industrial capacities of the least developed countries?

18. He felt that recent developments, including the reduction of most-favoured-nation (MFN) rates resulting from the Uruguay Round, the considerable progress achieved by certain developing countries in 1970-1980, the increasing number of free-trade agreements and trading blocs in the American continent and in Europe, made it necessary to take a second look at the GSP from the point of view of its objectives and operation. However, the replies to the secretariat questionnaire showed that the rules of origin continued to create obstacles and major difficulties for enterprises in beneficiary countries as to the choice of production processes. It was important at this stage to study carefully the differences between the harmonized WTO non-preferential rules and those of the GSP to determine to what extent the results of the former could be adapted in the case of the latter.

19. The representative of **New Zealand** stated that his Government employed the percentage criterion. It had recently issued a discussion paper that analysed the different means of determining origin and considered whether there was

scope for amending or changing the rules of origin. The New Zealand Government allowed global cumulation of origin, as well as donor-country content, and permitted the goods of beneficiary countries to enter the commerce of other beneficiary countries. With regard to documentary evidence, he stated that New Zealand had not been requiring the use of Form A since 1991.

20. The representative of the **United States of America** observed that, while the United States' GSP Scheme had 140 beneficiary countries, only about one third of those countries appeared to be represented in the Group of Experts. Furthermore, it was his understanding that very few countries had responded to the secretariat's questionnaire. He therefore wondered whether there was really a significant problem to be resolved or whether the Group of Experts was about to launch into an academic exercise.

21. The representative of the **World Customs Organization** stated that its Technical Committee on Rules of Origin had started its work in February 1995 and that the second session would take place in September 1995. He pointed out that the Agreements on Rules of Origin imposed the definition of the substantial transformation through the adoption of the change in tariff-heading criterion. He underlined that any other criteria should be used and applied only if the change in tariff heading did not allow for the definition of substantial transformation.

22. The representative of **Colombia**, responding to the comments made by the representative of the United States of America, said that the relatively limited attendance of developing beneficiary countries in the Group of Experts was due, in large measure, to the fact that many of these countries could not afford to finance the participation of experts from their capitals. It was most important to realize that this fact did not indicate a lack of interest in the subject of rules of origin on the part of these countries. On the contrary, the GSP schemes were helping the developing countries to achieve economic growth and sustainable development and she considered that the work of the Group of Experts was of the highest importance. She recalled that, in the past, the UNCTAD secretariat had often provided resources to enable developing country experts to participate in this type of meeting, and in this regard she called upon the developed countries to provide the necessary resources for this purpose.

23. The representative of the **United Republic of Tanzania** said that the least developed countries suffered not only from a limited industrial base and export capacities, but that they also continued to face substantial problems in many areas of origin rules due to their restrictiveness and administration. In this respect, special arrangements, suitable to their export capacities, should continue to be granted to the least developed countries to enable them to take full advantage of the GSP. He added that, although his country had not replied to the secretariat questionnaire, the replies given by the other countries would allow the Group to reach successful conclusions.

24. The representative of **Mexico** said that, in certain cases, origin criteria limited the export possibilities under the GSP of some products that underwent a substantial transformation without involving a change of tariff heading. Chemical products were an example. She pointed out that, as far as documentation was concerned, the invoice that arrived in the country of destination attached to the certificate of origin in some cases was not the one issued by the beneficiary country, but was in fact issued by trading houses in third countries. In that case, she considered that the certificate of origin should be accepted as sufficient proof of origin and that reinvoicing and intermediate trading should be allowed.

25. She considered that the process criterion and the percentage criterion were equally important and, depending on the products concerned, it might be more convenient to utilize one or the other. On the other hand, different origin criteria for the same products created problems for the textile, clothing and steel industries. For example, in order to comply with the strict origin requirements of the European Union, as compared to other countries, some carpet producers had had to switch their source of imports. Some countries of Eastern Europe accepted that the value of imported inputs should not exceed 50 per cent of the f.o.b. price and that, in the case of the United States, at least 35 per cent must be represented by local content. Before NAFTA had entered into force, the GSP scheme of the United States had been much more flexible than other schemes because, under the GSP scheme, Mexico could more easily export products like carpets, non-woven fabrics, steel plates, etc., but the same products did not qualify for preferential treatment from the European Union. Finally, the European Union legislation on GSP rules of origin required that certifying authorities in beneficiary countries must strictly control the issuance of certificates of origin. Because of this requirement, some trading houses established in Mexico that were not producing the goods that they exported could not benefit from the GSP since they were unable to supply the information required for a certificate of origin. On the other hand, Mexico had taken advantage of donor-country content under Japan's scheme. She requested that this facility be implemented by other preference-giving countries and that the regional or subregional cumulation should be extended to Mexico.

26. The representative of **Zimbabwe** stated that his country was seeking to widen its export markets and to benefit from GSP benefits. A single and unified set of rules of origin was therefore of fundamental importance to facilitate the task of compliance for producers and exporters.

27. The representative of **Nepal** expressed his appreciation for this opportunity to discuss the various aspects of the GSP and to learn more about its operational aspects. He pointed out that Nepal had not been able to exploit fully the donor-country content provisions and that technical assistance in this area would be beneficial to his country.

28. The representative of **Cuba**, noting that the main objective of the Group of Experts was to achieve harmonization of the GSP rules of origin, said that in the Uruguay Round Agreement, the common principle had been established, but there was no programme for harmonization of GSP rules of origin. She considered that the simplification of GSP rules of origin would contribute to the transparency of these rules and to the revitalization of the GSP.

29. The representative of **Canada** outlined the changes that her country was considering for its administration of the GSP scheme. In an effort to ease the administrative burden associated with the certification process, alternative certification methods were being studied. Consideration was being given to the acceptance of blanket Form A certificates of origin to prove entitlement to the GSP. Under this approach it would be possible for a single Form A to cover all shipments of identical goods that would occur in a specified period of up to one year. Moreover, the necessity for Form A to be certified by a certifying body in every case was being reviewed. It was expected that the direction of the review on these methods of certification would be defined by October 1995, when the Special Committee on Preferences held its next session.

30. She stated that, in response to representations concerning consignment provision made through UNCTAD's questionnaire, her country was prepared to waive the completion of the consignee in box 2 of Form A, when it was not commercially possible. This change was expected to be implemented with the publication of new guidelines in the autumn of 1995. The new guidelines would explain Canada's treatment of intermediate materials in the application of the origin content requirement. Under the Canadian scheme, qualifying content included the whole value of originating intermediate materials or the originating portion of non-originating intermediate materials. She added that in December 1992 a rulings programme had been formalized that provided advance decisions on the eligibility of specific products under various sets of rules of origin, including the GSP. Minor modifications might be made to this programme to ensure that Canada's obligations under aspects of annex II of the Agreement on Rules of Origin were satisfied.

31. In conclusion, she said that the administration of Canada's scheme was straightforward. Other than the clarifications that would be published in the autumn and the steps being taken to simplify the administrative aspects of the Canadian scheme, it was considered premature to look at other significant changes. Consideration of harmonized rules of origin would take place upon conclusion of the WTO exercise.

32. The representative of **Japan** said that the GSP objective of applying preferential tariff rates to products of developing countries with a view to promoting their economic development through exports confined GSP treatment to products either entirely produced or substantially transformed in GSP beneficiaries. He supported the views expressed by the representative of the European Community.

33. The representative of **Ethiopia** stated that his country could not send an expert to participate in the Group of Experts owing to lack of finances. As the outcome of this group would be an input to the Policy Review of the GSP, it was necessary that a special fund be established to finance the participation of experts from preference-receiving least developed countries. He added that his country attached great importance to technical assistance for training experts in this area.

34. The representative of the **World Trade Organization** (WTO) stated that the work programme on harmonization would officially start on 20 July 1995. The Technical Committee would conclude the whole process within two and a half years. The WTO Committee would meet in November 1995 to review the Technical Committee's work and the Technical Committee would report every quarter on the progress made in elaborating the Harmonized Set of Rules of Origin.

35. The representative of **India** said that developing countries had benefited from GSP preferential tariffs, for their GSP exports had increased at a higher rate than all other exports. Recent developments, such as the erosion of the preferential margin following the conclusion of the Uruguay Round, other commercial policy instruments and graduation, had called in question the usefulness of the GSP. Moreover, strict rules of origin represented an obstacle to the utilization of the GSP benefits. Therefore, the erosion of preferential margins no longer justified stringent criteria, since risks of trade diversion, as well as the possible use of origin to safeguard the interests of domestic producers, had been substantially reduced. However, there was a need for harmonization, simplification and improvement of the rules of origin. The adoption of a single criterion applicable under all GSP schemes would be a major step towards simplification. He considered that the process of harmonization of GSP rules of origin had to take place using the same criteria adopted in the Uruguay Round Agreement with regard to non-preferential rules of origin. However, the criteria formulated by the Technical Committee of the World Customs Organization would need to be adapted and made more liberal for GSP rules of origin.

36. The spokeswoman for the **Group of 77 and China** (Colombia) said that, having heard the useful explanations and clarifications by the secretariats of the World Customs Organization and the World Trade Organization, the Group of 77 and China were now in a position to better appreciate the technical character of the work to be carried out by the World Customs Organization, which would concentrate on the definition of substantial transformation utilizing the change of tariff heading criterion. She believed that this work should form the basis for the possible harmonization of GSP rules of origin.

37. In view of the ongoing debate, the Group of 77 and China wished to support the conclusions and recommendations put forward by the UNCTAD secretariat in TD/B/SCP/AC.1/2. In particular, the UNCTAD secretariat should

attend the meetings of the Technical Committee established in the World Customs Organization and report annually on the progress made to the Special Committee on Preferences. It was extremely important that States members of UNCTAD be given the opportunity to appreciate and discuss periodically in the Special Committee on Preferences the progress made on harmonizing non-preferential rules of origin rather than being confronted with a final text as approved by the Council of the World Trade Organization. This would allow both preference-giving and preference-receiving countries to assess the results and examine the possibility of translating them into the GSP context. It was generally agreed that, whereas WTO was a rule-setting organization, UNCTAD was a forum for consensus-building and debate, with a larger membership that attached great importance to rules of origin. Furthermore, UNCTAD was an organization which provided delegations with detailed studies. As well as having educational value for the developing countries, such documents provided negotiating leverage in WTO. It was surely of benefit to both developed and developing countries to have well-informed negotiations. For these and other reasons, her Group and China believed that the review of the negotiating process for the rules of origin in this Group of Experts should take place in collaboration with WTO - a process that was vital for the development of the developing countries.

38. Finally, the Group of 77 and China attached great importance to the content of the Common Declaration contained in the Uruguay Round Agreement, especially in the matter of the binding origin information and the possibility of judicial review of origin determination. Such improvements could help to lend stability, predictability and legal certainty to origin determination. In this context, the preference-giving countries could perhaps explain how they were going to implement such commitments.

Action by the Intergovernmental Group of Experts

39. At its 4th (closing) meeting, on 21 July 1995, the Intergovernmental Group of Experts adopted the draft agreed conclusions on agenda items 3 and 4, circulated in TD/B/SCP/AC.1/L.2, with minor amendments (for the agreed conclusions, see annex I below).

## Chapter II

## ORGANIZATIONAL MATTERS

### A. Opening of the session

40. The session of the Intergovernmental Group of Experts on Rules of Origin was opened on 19 July 1995 by Mr. F. Abbate, Officer-in-charge of the International Trade Division of UNCTAD.

### B. Election of officers

(Agenda item 1)

41. At the opening meeting, on 19 July 1995, the Intergovernmental Group of Experts on Rules of Origin elected the following officers to serve on its Bureau:

| | | |
|---|---|---|
| Chairman: | Mr. Philip Nell | (Switzerland) |
| Vice-Chairman-cum-Rapporteur: | Mr. Yan Ayub | (Indonesia) |

### C. Adoption of the agenda

(Agenda item 2)

42. At the same meeting, the Intergovernmental Group of Experts adopted its provisional agenda (TD/B/SCP/AC.1/1) as follows:

1. Election of officers
2. Adoption of the agenda
3. Consultations on harmonization of the rules of origin
4. Consultations on simplification and improvement of the rules of origin
5. Other business
6. Adoption of the report of the Intergovernmental Group of Experts on Rules of Origin.

### D. Adoption of the report of the Intergovernmental Group of Experts on Rules of Origin

(Agenda item 6)

43. At its 4th (closing) meeting, on 21 July 1995, the Intergovernmental Group of Experts adopted its draft report (TD/B/SCP/AC.1/L.1 and Add.1), with minor amendments, and authorized the Rapporteur to complete the report in the light of the proceedings of the closing plenary.

ANNEXES

**Annex I**

CONSULTATIONS ON HARMONIZATION OF THE RULES OF ORIGIN

CONSULTATIONS ON SIMPLIFICATION AND IMPROVEMENT OF THE RULES OF ORIGIN

Agreed conclusions of the Intergovernmental Group of Experts on Rules of Origin

1. In accordance with its terms of reference, the Intergovernmental Group of Experts on Rules of Origin met on 19 to 21 July 1995 to make proposals to the Special Committee on Preferences, in view of the policy review on the GSP in 1995, on the harmonization, simplification and improvement of the rules of origin. The Intergovernmental Group of Experts reached the following conclusions:

## I. Harmonization of rules of origin

2. With a view to progressing towards the harmonization of GSP rules of origin, and recognizing the importance and value of the work to be undertaken by the Technical Committee established within the World Customs Organization, the Intergovernmental Group of Experts on Rules of Origin recommends that the Special Committee on Preferences adopt the following text at its twenty-second session:

The UNCTAD secretariat is requested to:

(a) Follow and monitor, as an observer, the work carried out within the Technical Committee and, when appropriate, contribute to the technical aspects of this work;

(b) Report annually to the Special Committee on Preferences on the progress made and results achieved by the Technical Committee with a view to progressing towards harmonization of the GSP rules of origin;

(c) Propose, once the Technical Committee has achieved its objectives and taking due account of the WTO's work, a harmonized set of rules of origin, including modifications and amendments where appropriate, to UNCTAD member States, for their consideration and adoption.

## II. Simplification and improvement

### A. Cumulation

3. Some preference-giving countries grant partial or full cumulation for regional groupings. In the past few years, several regional groupings have

strengthened their relationships and new groupings have been created. Moreover, preference-receiving countries emphasized the importance of global cumulation.

Recommendation: Improvements in the rules of origin should be sought by expanding global or regional cumulation and its scope to additional or newly formed regional groupings. To this end, the secretariats of these regional groupings may request to be granted regional cumulation, according to the provisions laid down by the preference-giving countries.

### B. Relaxation of stringent rules of origin

4. Some rules of origin have requirements which may be met only with great difficulty and limit the efficient sourcing of inputs.

Recommendation: Improvements and simplification of such rules should be sought to facilitate their use by preference-receiving countries.

### C. Direct consignment

5. For some preference-receiving countries, especially land-locked countries, the direct consignment requirements hamper the utilization of GSP benefits. These requirements do not take into account the possibility of intermediate trading. In particular, when exported goods are in transit in a third country, the customs authorities in the country of transshipment usually do not issue the required documentary evidence. In some cases the exporters are not in a position to know the final destination of the goods as the transactions are being made by trading houses which do not reveal the name of the final consignee.

Recommendation: Improvements in the system for countries facing direct consignment problems should be sought through adequate arrangements with preference-giving countries with regard to alternative means of documentary evidence.

### D. Least developed countries

6. Several preference-giving countries have special programmes to relax rules of origin for LDCs.

Recommendation: Improvements for LDCs should be sought within the existing arrangements provided by some preference-giving countries by allowing that the request for derogation be made by certifying authorities.

### E. Binding origin information and judiciary review

7. The Intergovernmental Group of Experts on Rules of Origin noted the value of the commitment made by preference-giving countries within the Common Declaration on Preferential Rules of Origin of the WTO Agreement on Rules of

Origin. In this context, the Intergovernmental Group of Experts recommends the consistent implementation of the provisions contained in Article 3, paragraphs (d) and (f) of the Common Declaration.

The implementation of this commitment will contribute to imparting transparency, stability and legal certainty to origin determination.

## F. Administrative cooperation between donor countries and receiving countries

8. The functioning of the GSP can be improved with enhanced administrative cooperation between preference-giving and receiving countries for ex-post controls, meeting deadlines and reliability of the information provided in the origin certificates.

## G. Administrative procedures

9. Consideration should be given to abolishing Form APR and to accepting a simple certification made by the exporter on the invoice as sufficient proof of origin status.

10. The notes on the back of GSP Form A should be modified as follows:

(a) European Economic Community should be replaced by European Community;

(b) Austria, Finland and Sweden should be listed under the European Community and should be deleted from Note III.3.

(c) Union of Soviet Socialist Republics should be replaced by Russian Federation;

(d) Czechoslovakia should be replaced by Czech Republic and Slovakia;

(e) The note marked with asterisks concerning the United States should be replaced by an insertion in the text as follows: "The United States does not require GSP Form A. A declaration setting forth all pertinent detailed information concerning the production or manufacture of the merchandise is considered sufficient only if requested by the District Collector of Customs";

(f) The old stock of GSP Form A should remain valid until 31 December 1997;

11. During discussions on the need to maintain the requirement of GSP Form A and the quality of its paper, several preference-giving countries stated that they no longer required GSP Form A since it had been replaced either by computerization or by a declaration made by the importer. However, other preference-giving countries wished to maintain the present rules as they were of the opinion that GSP Form A was necessary in order to avoid fraud and counterfeiting and to facilitate any verification procedure which their authorities might carry out.

## Annex II

## ATTENDANCE 1/

1. The following States members of UNCTAD were represented at the session:

Albania
Algeria
Argentina
Austria
Bolivia
Bulgaria
Canada
China
Colombia
Cuba
Czech Republic
Democratic People's Republic of Korea
Ecuador
Egypt
El Salvador
Ethiopia
Finland
France
Germany
Honduras
Hungary
India
Indonesia
Iran (Islamic Republic of)
Italy
Japan
Madagascar
Mali
Mexico
Morocco
Nepal
Netherlands
New Zealand
Pakistan
Qatar
Republic of Korea
Romania
Russian Federation
Saudi Arabia
Slovakia
Spain
Sri Lanka
Sweden
Switzerland
Thailand
Turkey
United Kingdom of Great Britain and Northern Ireland
United Republic of Tanzania
United States of America
Venezuela
Zimbabwe

2. The European Community was also represented.

3. The following other State member of UNCTAD was represented as observer at the session:

Andorra.

4. The following specialized agency was represented at the session:

International Monetary Fund.

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1/ For the list of participants, see TD/B/SCP/AC.1/INF.1.

5. The World Trade Organization was also represented.

6. The following intergovernmental organizations were represented at the session:

Organization for Economic Cooperation and Development
World Customs Organization

7. The following non-governmental organizations were represented at the session:

General category

Association of European Chambers of Commerce and Industry
International Chamber of Commerce
International Federation of Business and Professional Women

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(311)

**UNITED NATIONS**

**TD**

United Nations Conference on Trade and Development

Distr.
GENERAL

TD/B/SCP/15
23 June 1995

Original: ENGLISH

TRADE AND DEVELOPMENT BOARD
Special Committee on Preferences
Twenty-second session
Geneva, 23 October 1995
Item 3 of the provisional agenda

# REVIEW OF THE IMPLEMENTATION, MAINTENANCE, IMPROVEMENT AND UTILIZATION OF THE GENERALIZED SYSTEM OF PREFERENCES, RULES OF ORIGIN AND TECHNICAL ASSISTANCE

## Report of the Second Ad Hoc Expert Group on the Generalized System of Preferences (15-16 May 1995)

submitted to the Officer-in-Charge of UNCTAD

GE.95-52284

## PART I: PROCEEDINGS

1. The Ad Hoc Expert Group on the Generalized System of Preferences was convened by the Secretary-General of UNCTAD in pursuance of the request made by the Special Committee on Preferences at its twentieth session to start preparations for theG3 1995 Policy Review on GSP and "to prepare in-depth analytical studies on the possibilities for improving the functioning and enhancing the impact of the GSP in the light of the evolution of the international economic and political environment".[1] In preparing these studies, the Secretary-General was invited to consider "the advice of senior GSP experts, eminent personalities in international economics and international trade, academics or representatives of the business communities, from both developed and developing countries".[2]

2. The first meeting of the Ad Hoc Expert Group took place on 24 and 25 February 1994. It examined the GSP issues on the basis of the draft documentation prepared by the secretariat to be submitted to the twenty-first session of the Special Committee on Preferences[3] and submitted a report on its deliberations to the Secretary-General of UNCTAD.[4] The report was subsequently submitted to the twenty-first session of the Special Committee on Preferences, which requested the secretariat to prepare complementary studies and reviews in the light of the Chairman's summary.[5]

3. The Second Ad Hoc Expert Group was held on 15 and 16 May 1995 in order to follow up on the first meeting and to have a more detailed discussion of the subjects addressed. It had before it the following draft documentation prepared by the secretariat and UNCTAD consultants to be submitted to the twenty-second session of the Special Committee on Preferences: (i) Study on harmonization, simplification and improvement of the rules of origin: Options and proposals for harmonization, simplification and improvement of the rules of origin (TD/B/SCP/AC.1/2); and Summary of replies received from preference-giving and preference-receiving countries to the questionnaire prepared by the UNCTAD secretariat (TD/B/SCP/AC.1/2/Add.1); (ii) Draft study on criteria for graduation under the generalized system of preferences; (iii) Resumé of UNCTAD study on the impact of the erosion of the preferential margin resulting from the Uruguay Round tariff reductions on the trade of developing countries; (iv) Resumé of study on possible extension of the GSP concept to new areas, in particular, services and investment; and, (v) The Least Developed Countries 1995 Report, Part B - the Generalized System of Preferences and LDCs.

4. The list of experts, who participated in their personal capacities, is contained in the annex.

## PART II: CONCLUSIONS AND RECOMMENDATIONS

5. At its closing meeting, on 16 May 1995, the second Ad Hoc Expert Group agreed on the following conclusions and recommendations:

### Objectives

6. The experts discussed the objectives of the GSP, namely to increase export earnings, to promote industrialization and to accelerate economic growth, and whether they remained fully valid in the light of the developments which had taken place over the years in world trade and related political realities. Some experts felt that the objectives remained valid but should be strengthened within the actual GSP framework by an expansion of product coverage and deeper tariff cuts. Other experts said that, in order to revitalize the GSP, the concept underlying the present objectives of the system should be expanded to include other development objectives such as social and environmental concerns. The latter aspects could eventually develop a second generation of GSP schemes with possible expansion of product coverage and additional preferences. Some experts questioned the appropriateness of such other development objectives given the autonomous nature of the schemes and said any new objectives should be multilaterally agreed.

### Product coverage

7. There was broad consensus that an expansion of product coverage should be considered for the revitalization of the GSP, due to the fact that only a quarter of all dutiable exports benefited from the GSP.[6] One expert emphasized that since eligible product exports under future GSP schemes would be affected by various trade remedy measures, such as safeguards, graduation and special safeguards for agriculture, and the average level of MFN rates would be gradually reduced by staging, there should be no major obstacles to having a broadened product coverage.

### Graduation

8. The experts noted the background study "Criteria for graduation under the GSP" which provided a framework for discussion together with suggested criteria for graduation.

(a) <u>The concept of graduation</u>

9. The concept of graduation in the context of GSP is to provide for the withdrawal of GSP treatment when it is no longer warranted. Graduation should be based on objective criteria related to the multilaterally agreed objectives of the GSP. Graduation measures should be independent from safeguard measures.

10. The rationale for graduation includes: (i) to provide incentives for the transfer of GSP benefits from more advanced to less advanced beneficiary countries; and (ii) to facilitate the improvement of GSP schemes for the remaining beneficiary countries.

11. There was agreement that there existed two basic graduation concepts: partial graduation and full graduation. However, there were differing views on each of these concepts. Some experts felt that only full graduation was appropriate; others that only partial graduation was appropriate; still others said that the two concepts were complementary.

12. There was agreement that graduation, when warranted, was a reflection that the beneficiary subject to graduation was successful. However, there were several views about what success meant in the light of the objectives of the GSP. Partial graduation was sometimes referred to as product-country graduation and sometimes referred to as sector-country graduation. One expert stressed that partial graduation should reflect the successful industrial development in one or more sectors in the beneficiary country, the exports of which are competitive in international markets. In this case, partial graduation would eliminate GSP treatment for all products in that sector. Some other experts felt that partial graduation could be justified for more narrowly defined products provided that graduation reflected the successful exportation of the product vis-à-vis all other suppliers, including non-beneficiary countries.

13. There was general agreement that graduation must be based on objective criteria. Some experts felt that the appropriate criteria might depend upon specific conditions in the individual preference-giving countries. Some experts felt the criteria should be limited to trade-related indicators while others felt the criteria should be broadened to include more general development indicators. All experts agreed that there should be no "conditionality", or element requiring reciprocal action, associated with graduation criteria, either for partial graduation or for full graduation.

14. Graduation can be phased in by eliminating GSP treatment on products competitively exported by particular beneficiary countries. A second graduation concept would be to fully withdraw GSP treatment on all products exported by a particular beneficiary country. In the first concept, the beneficiary subject to graduation continues to enjoy GSP treatment on other products or other sectors. In this connection, an expert said that so-called graduation related to competitive exports of individual products is not a proper graduation mechanism as it can only be based on trade criteria and not on development criteria and consequently is more a safeguard type mechanism. In the second concept, the beneficiary subject to graduation no longer enjoys GSP treatment on any product exported to the preference-giving country.

15. A number of experts proposed that the more advanced developing countries should consider becoming preference-giving countries to benefit the less advanced beneficiary countries. One expert said that consideration of the subject was premature and pointed to the existence of the global system of trade preferences among developing countries (GSTP).

(b) Principle of neutrality

16. Graduation should not have a significant adverse effect on exports from a graduated beneficiary country.

17. Graduation should not reduce the total volume of GSP benefits. Empirical evidence has revealed that prior graduation has resulted in very little benefit for the remaining beneficiary countries. Since graduation will reduce GSP benefits enjoyed by the beneficiary subject to graduation, GSP benefits enjoyed by the remaining beneficiary countries, effectively using these new opportunities, should be increased by an offsetting amount.[7]

(c) Operational aspects

18. Graduation, when introduced, should include a grace period or phase-in period, as appropriate. Uncertainty should be avoided to the greatest extent possible. Graduation measures should not result in a product being eliminated from GSP for one year, to be restored the next, to be eliminated the next, etc. Graduation should be based on multi-year criteria.

**Erosion**

19. The experts welcomed the MFN tariff reductions deriving from the successful conclusion of the Uruguay Round and took note of the preliminary estimates by the UNCTAD secretariat of the erosion of the preferential margin resulting from these reductions. They agreed that erosion of tariff preferences resulting from these overall MFN tariff reductions is not in itself a negative phenomenon.

20. Several proposals were made to mitigate this adverse effect, including the reduction of GSP tariffs, expansion of product coverage and improvement of the mechanism of the system. Of these, it was felt that one of the best ways would be to expand product coverage.

21. As the secretariat's study on erosion was at a preliminary stage, it was suggested that the study be continued and, where possible, focus on the following elements:

- estimates of the average level of GSP rates;
- identification of major export sectors where the preferential margin becomes zero;
- the impact of erosion by region;
- identification of non-GSP covered products (by product category) which are of export interest to developing countries; and,

- estimates of the possible trade effects resulting from the Uruguay Round tariff concessions on trade flows of developing countries.

**Special measures in favour of least developed countries**

22. There was general consensus that special measures for LDCs should be strengthened in the light of the Uruguay Round results. To this end, the Group reaffirmed the recommendation made at its first meeting, namely full product coverage, full duty-free GSP rates, and exemption from safeguards and from graduation measures.

**Possible extension of the GSP concept to new areas, in particular, services and investment**

23. The Group discussed the study on new areas currently being prepared by UNCTAD consultants. The main points are summarized below:

(a) Services

24. The General Agreement on Trade in Services sets out principles to govern trade in this area, extending the MFN principle to trade in services. It is important that specific areas be identified in which it would be feasible to consider measures equivalent to the GSP to increase demand for service exports from developing countries arising from the possible extension of the GSP concept to services. This will involve: (i) identification of sectors in which developing countries have a comparative advantage; (ii) identification of policies in developed countries which regulate the importation of services in these sectors; (iii) identification of means by which these policies might be adjusted in order to promote consumption of services produced by developing countries. There was some disagreement as to which sectors were the most likely candidates for such an analysis, especially in the area of labour services. The study will attempt to provide a comprehensive list of sectors in which policy adjustment might feasibly be considered.

(b) Investment

25. Two issues arose:

(i) It may be possible to identify adjustments to the existing policy regime by which the authorities of a developed country might stimulate investment in developing countries. However, questions were raised as to whether such adjustments would fall into the category of GSP, even if this term were extended to cover trade measures other than tariffs and quotas.

(ii) Some developing countries have introduced measures to subsidize foreign investment in the domestic economy, or to extract greater domestic benefit from such investment (for example, some types of TRIMS). To the extent that the TRIMS Agreement restricts such measures, preferential treatment to developing countries would mean allowing them to retain investment promotion measures and TRIMS. However, questions were raised as to whether such preferences would be welfare-improving. Furthermore, those preferences would not be a GSP-like preference but would have to be set in terms of special and differential treatment within TRIMS.

**Rules of origin**

26. The experts supported, in principle, the proposals put forward by the secretariat in TD/B/SCP/AC.1/2, including the suggestion that the work of the World Customs Organization (WCO) Technical Committee might be taken into account when developing a harmonized set of GSP rules of origin. The experts recommended that this issue be further dealt with at the Intergovernmental Group of Experts on Rules of Origin to be held in Geneva from 19 to 21 July 1995.

27. It was felt that an application of a single set of rules would be desirable vis-à-vis both non-preferential and preferential trade as it would be beneficial for GSP users, certifying authorities and customs authorities in preference-giving countries. However, owing to the different objectives for the harmonization of non-preferential rules of origin as compared to GSP rules of origin, some experts pointed out that the UNCTAD secretariat should continue its work on rules of origin; the work on GSP rules of origin should be linked to the GSP objectives and not constrained by considerations dealt with in other contexts or frameworks.

28. There was a consensus that the erosion of the preferential margin following the conclusion of the Uruguay Round called for simplification and improvement of the GSP rules of origin if the economic significance of the system was to be assured. The linkages between graduation and cumulation were also discussed. It was felt that country graduation measures which were or might be applied in the context of cumulative origin might undermine the efforts of preference-receiving countries to globalize their sourcing of inputs in manufacturing GSP-eligible products.

29. Improvement and simplification of GSP rules of origin could be made by simplifying rules on administrative procedures, such as GSP Form A and the direct consignment rules. Some experts emphasized the importance of administrative cooperation based on mutual confidence between certifying authorities in beneficiary countries and customs authorities in preference-giving countries on certification and verification.

**Technical assistance**

30. There was consensus that the GSP technical cooperation programme was useful and should be continued. The experts were satisfied that the programme had implemented the actions recommended by the first Ad Hoc Expert Group Meeting, such as cost-sharing and emphasis on rules of origin and trade laws. In order to further improve the activities, the Group recommended that:

(a) the programme should revise as a matter of priority the present handbooks on individual GSP schemes and other trade laws to reflect changes resulting from the implementation of the Uruguay Round Agreements;

(b) in carrying out its activities, the programme should put more emphasis on national seminars/workshops which provided a better opportunity for direct contacts with actual and potential GSP users; and

(c) the programme should consider other possibilities of providing technical assistance such as South-South cooperation or a technical cooperation among developing countries (TCDC) element, and use of trade points to disseminate GSP information.

## Notes

1. Report of the Special Committee on Preferences on its twentieth session (TD/B/40(1)/10), annex I, para.1.

2. Ibid., para. 2.

3. Documents considered by the Ad Hoc Expert Group Meeting were:

- Seventeenth general report on the implementation of the generalized system of preferences: recent changes and policy issues (TD/B/SCP/6);

- Technical assistance in connection with the GSP - Technical cooperation activities on the GSP and other trade laws, 1993 (TD/B/SCP/7);

- Consultation on harmonization and improvement in the rules of origin - review of past discussions: recent developments; possible ways forward (TD/B/SCP/8);

- Possible improvements of the generalized system of preferences (UNCTAD/ITD/8).

4. Report of the Ad Hoc Expert Group on the Generalized System of Preferences (TD/B/SCP/9).

5. See the report of the Special Committee on Preferences on its twenty-first session (TD/B/SCP/10), annex I.

6. See the seventeenth general report on the implementation of the generalized system of preferences (TD/B/SCP/6), annex I.

7. An expert suggested that the amount of GSP benefits be measured as the tariff revenue forgone by the preference-giving countries on imports receiving GSP treatment.

Annex

**List of participating experts**

- Mr. C.M. Bicalho Cozendey, Second Secretary
  Permanent Mission of Brazil
  Geneva, Switzerland

- Dr. D. Fielding
  Department of Economics
  University of Nottingham
  United Kingdom

- Mr. P.K. Mohanty, Deputy Secretary
  Ministry of Commerce
  New Delhi, India

- Dr. T. Murray, Distinguished Professor
  University of Arkansas
  Fayetteville
  United States of America

- Mr. M. Nampa, First Secretary
  Permanent Mission of Japan
  Geneva, Switzerland

- Mr. P. Nell, Head
  Services of Origin
  Federal Office for Foreign Affairs
  Bern, Switzerland

- Mr. F. Nizery, Head
  GSP Section
  EC Commission
  Brussels, Belgium

- Mr. J. Onishi, Senior Deputy Director
  Customs and Tariff Bureau
  Ministry of Finance
  Tokyo, Japan

- Mr. D. Satherstrom, Chief
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  Department of Finance
  Ottawa, Canada

- Mr. P. Waer, Partner
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